

**NOTICES OF AUDITORS LEAVING
OFFICE**

Consultation on
simplification for companies
and auditors

NOVEMBER 2009

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Notices of auditors leaving office

The auditor of a company can leave office for many reasons. In some cases, this is a normal part of business; the company may no longer need an audit, they may decide to retender, or the auditor may retire. In other cases, the departure may be the result of a disagreement between company and auditor, or a situation which raises questions about the conduct of the company's affairs. At the moment, even in many of the most routine cases, the audit authorities have to be notified, and reasons provided. Notifications and statements of reasons may also need to be filed with Companies House.

This document invites comments on the options for simplifying the arrangements for the provision of information to shareholders, creditors, the audit and accounting authorities and Companies House when auditors leave office.

The present arrangements are a combination of measures put in place under the successive Companies Acts to provide information to shareholders and Companies House, and measures introduced in 2006 to meet the requirements of the EU Audit Directive for the provision of similar information to the audit regulatory bodies.

In the Government's view, after 18 months of operation of the current system, the arrangements may be more complex than necessary and are potentially duplicatory. This document identifies areas for possible simplification and streamlining while still meeting the UK's obligations under the Directive and the underlying policy goals.

Issued: 25 November 2009

Respond by: 20 January 2010

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This consultation is relevant to: auditors; audit and accountancy bodies; and companies, shareholders and investors.

1. Executive Summary

This document invites comments on the options for simplifying the arrangements for the provision of information to shareholders, creditors, the audit and accounting authorities and Companies House when auditors leave office.

The present arrangements are a combination of measures put in place under the successive Companies Acts to provide information to shareholders and Companies House, and measures introduced by the Companies Act 2006 to meet the requirements of the EU Audit Directive for the provision of similar information to the audit authorities.

In the Government's view, after 18 months of operation of the current system, the arrangements may be more complex than necessary and are potentially duplicatory. This document identifies areas for possible simplification and streamlining while still meeting the UK's obligations under the Directive and the underlying policy goals. The Government would welcome views of companies, auditors, investors and other stakeholders on whether these proposals should be taken forward.

The document seeks views on:

- removing the duty to notify audit authorities of an auditor's departure in some cases where it is of little interest to those authorities;
- removing the duty on the audit authorities to notify the accounting authorities of all auditor departures of which they are informed;
- whether there should be any changes to requirements for information to be provided to investors when auditors leave listed companies;
- removing the need for companies to notify Companies House in certain cases of auditor departure;
- simplifying the legislation by clarifying definitions.

Although the potential savings are relatively modest, the Government believes there is value in streamlining these provisions after experience of their operation, so that unnecessary burdens can be removed, particularly from smaller businesses, and the provisions can be effectively focussed on the information of real value.

2. How to respond

When responding to this consultation please state whether you are responding as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.

A copy of the consultation questions is available electronically at <http://www.bis.gov.uk/consultations>. Your response can be submitted by letter, fax or email to:

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Consultees

This consultation is relevant to: auditors; audit and accountancy bodies; and companies, shareholders and investors. A list of those organisations and individuals consulted is at Annex B. We would welcome suggestions of others who may wish to be involved in this consultation process.

The consultation is UK wide. The Northern Ireland administration has agreed that, while company law remains a transferred matter within the legislative competence of the Northern Ireland Assembly, the Companies Act 2006 should apply to the whole of the UK. Consequently any changes to company law resulting from this consultation will apply UK-wide.

Timing

This consultation runs for eight weeks from 25 November 2009 until 20 January 2010. This reflects the fact that the Government has already discussed these issues with many of the groups most directly affected. Ian Lucas, Minister for Business and Regulatory Reform, has agreed to consult on these legislative proposals for less than twelve weeks.

3. Additional copies

You may make copies of this document without seeking permission. Further printed copies of the consultation document can be obtained by post from:

BIS Publications Orderline
ADMAIL 528
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An electronic version can be found at www.bis.gov.uk/consultations.

Other versions of the document in Braille, other languages or audio-cassette are available on request.

4. Confidentiality & Data Protection

Information provided in response to this consultation, including personal information, may be subject to publication or release to other parties or to disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004). If you want information, including personal data that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence.

In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

5. Help with queries

Questions about the policy issues raised in the document can be addressed to:

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A copy of the Code of Practice on Consultation is in Annex A.

6. Detailed Discussion

1. The present system

1.1 The present system for the provision of information about the departure from office of auditors is complex, and has arisen from a combination of domestic policy requirements and the need to comply with EU law. In the light of experience of these requirements, the Government wishes to explore the scope for streamlining them so that burdens are reduced, while the underlying policy objectives are still met, and the UK remains in compliance with EU law. This paper aims to provoke discussion by presenting some specific proposals for change.

Main elements

1.2 There are two main parts to the present system. The first part, which has evolved over successive Companies Acts, is a series of requirements for notifications from the company and the auditor to Companies House and to shareholders covering the fact that the auditor has departed and the circumstances around that departure. The second part, new to the Companies Act 2006, implements the EU Audit Directive¹ requirement in Article 38.2² for audit authorities³ to be notified, both by the company and the auditor of the departure of an auditor, and the reasons for it, when this occurs before the end of their term of office. There is a further requirement for the audit authorities to pass notifications, and in some cases the statement of reasons, onto the accounting authorities⁴.

1.3 The intentions of the two parts are slightly different. The original UK provisions are designed to provide the public, and in particular shareholders and creditors, with information around the circumstances of departure of an auditor from a company. The purpose of the EU Directive provisions is to provide the audit authorities with the reasons for an auditor's departure which might be relevant for them in their regulatory role. These provisions, which require the separate submission of views

¹ Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC.

² Article 38.2 states that "Member States shall ensure that the audited entity and the statutory auditor or audit firm inform the authority or authorities responsible for public oversight concerning the dismissal or resignation of the statutory auditor or audit firm during the term of appointment and give an adequate explanation of the reasons therefor".

³ The audit authorities are the Professional Oversight Board of the Financial Reporting Council (POB); and the Recognised Supervisory Bodies for auditors under Part 42 of the Companies Act 2006 (the ACCA, AAPA, ICAI, ICAS and ICAEW)

⁴ The accounting authorities are: the Secretary of State, so that information can be made available to Companies Investigations Branch (CIB), which is part of the Insolvency Service; and the Financial Reporting Review Panel (FRRP) which is part of the Financial Reporting Council.

from both the company and the auditor, are particularly focussed on situations where there may have been a dispute between the two parties. The additional forwarding onto the accounting authorities was designed to allow them to consider whether the circumstances of an auditor's resignation raise issues about a company's accounts.

1.4 The arrangements, at least as far as they applied to listed companies, were debated in 2004/05 by stakeholders as part of the work of the Audit Quality Forum⁵, and this debate fed into the way the provisions were handled in what is now the Companies Act 2006. There was particular concern at that time to ensure, in the case of listed companies, that shareholders were fully informed of the circumstances around an auditor's departure, as well as concern that the implementation of the EU Audit Directive should not water down what were felt to be important features of the UK system. These are important considerations. The question is whether, in the light of experience, they could be achieved in a more efficient way.

How it works

1.5 The essential features of the legislative framework for audits that are not major audits are set out here. In each case it is indicated whether this is a UK originating provision (UK) or one which originates from the EU Audit Directive (EU). Slightly different considerations arise for major audits, which are discussed in section 5, along with an explanation of how the present system operates in respect of these audits.

- When an auditor resigns or is removed by resolution of the members of a company, the company must notify Companies House (UK).
- Whether they leave office at or before the end of their term of office, the auditor must deposit a statement with the company of the circumstances connected with ceasing to hold office, or they may deposit a statement that there are no circumstances that need to be brought to the attention of shareholders and creditors (UK).
- If the auditor stated circumstances that needed to be brought to the attention of shareholders and creditors, and unless a court rules that the auditor's statement is seeking needless publicity for defamatory material, the company must circulate the statement to shareholders and creditors.
- Unless a court rules as above, the auditor must send a copy of their statement of circumstances (or any statement that there are no circumstances) to be filed at Companies House (UK).

⁵ see section 5 of chapter 6 for further discussion of the AQF report *Shareholder involvement – Auditor resignation statements*.

- The auditor must file a statement of reasons for their departure with the audit authority, if the departure was before the end of their term of office (EU). If the auditor issued a statement of circumstances, this must form the statement of reasons (UK).
- The company must also file a statement of reasons with the audit authority if the departure was before the end of the auditor's term of office (EU). This may be the auditor's statement of circumstances mentioned above (if the auditor stated circumstances), though the company may submit its own statement.
- The audit authority must notify the accounting authorities of the notices it receives of auditor departure, and may forward the statement of reasons (UK).

1.6 In practice, we understand that between them, the audit authorities currently receive in the region of 10,000 notifications per year from auditors, though the number from companies is considerably lower, raising questions about the level of compliance. Compliance by companies with the requirements to notify Companies House is higher, with around 8,500 notifications of auditor resignation filed each year, many of them attaching the auditor's statement of circumstances, even though this is not required to be filed by the company. In many cases, the reasons that the auditor has ceased to hold office appear to be routine, for example a decision by the company to take advantage of audit exemption or change to an auditor who also audits a parent company.

1.7 Even from the short description here, it is clear that these provisions are complex and arguably duplicatory. Concerns have also been expressed to the Government that aspects of them serve little useful purpose⁶, especially where the reasons for the departure of the auditor are uncontroversial. The Government has therefore identified a number of areas where it might be possible to reduce the burdens and complexity of the legislation, while still delivering its essential purpose and complying with the requirements of EU law. The proposals and issues are summarised in the next section and then discussed in full detail in turn.

⁶ eg by the Professional Oversight Board of the Financial Reporting Council in its annual report to the Secretary of State for Business, Innovation and Skills for the year ending 31 March 2009. The report is available at www.frc.org.uk/pob/publications/pub2030.html (see paragraphs 2.45 to 2.47 on page 19).

2. Approach to changes

Providing exemptions to the requirements to notify audit authorities

2.1 The first element of reform is to look at the part of the system which fulfils the EU Audit Directive requirement for notifications and statements of reasons to be sent by the auditor and the company to the audit authority. The concern has been expressed to us that the vast majority of the notifications received are of little if any regulatory interest, and reflect routine departures of the auditor in the normal course of business. For non-major audits, we therefore propose to exempt certain kinds of auditor departure which we believe are of little interest to the authorities and which do not reflect the underlying intention of the Directive.

2.2 At present, where the auditor sends to the company a statement of circumstances, the company is required to circulate it to its members and others entitled to receive the annual accounts. We are seeking views on whether, only in cases where the auditor requires circulation of a statement of reasons, would it need to be filed at Companies House.

Removing the requirements for notifications to be passed on to accounting authorities

2.3 Related to the first change is the proposal to remove the requirement for the audit authorities to pass on all the notifications they receive to the accounting authorities. It has become clear from 18 months of experience with the system that the routine forwarding of all notifications has little value, and considerable costs for the audit authorities in collating the data. The Government would therefore propose to repeal this provision. The Government does not intend to change the parallel arrangement by which audit authorities forward a smaller number of statements of reasons to the accounting authorities in cases which may be of regulatory interest, as this is proving useful.

Departures of auditors for major audits

2.4 In the case of major audits⁷ stakeholders felt (in 2005) that it was important for shareholders and creditors of a company always to receive the statement from the auditor as to the circumstances around their departure. This is a requirement additional to notifying the audit authority and goes beyond what is required by the EU Audit Directive. The Government would be interested in whether the 2005 view has changed, although for the present it has not made proposals for paring the

⁷ See sections 5 and 7 of this chapter for discussion of which companies are subject to major audit.

requirements back, beyond some minor adjustments which would relieve particular requirements on companies.⁸.

Removing the requirements for companies to notify Companies House

2.5 At present there are requirements for the company to notify Companies House when an auditor resigns or is removed by a resolution of members. It is not clear that great use is made of these notifications. The Government would appreciate receiving views on whether they serve a valuable purpose, but in the absence of clear evidence that they are important, the Government is inclined to remove the requirements.

Streamlining definitions

2.6 As the present requirements are the result of different initiatives at different times, there are inconsistent definitions in the Companies Act 2006. For instance, the requirements based on the EU Audit Directive distinguish between major and non-major audits, while the UK based requirements divide audits into those of quoted and non-quoted companies. The UK based provisions refer to “circumstances” connected with an auditor’s departure, while the EU based provisions require “reasons”. It is the Government’s intention to streamline these definitions, with the aim of making the provisions as a whole easier to understand.

⁸ See section 5 of this chapter for discussion of current administrative burdens that might be removed from companies subject to major audit.

3. Providing exemptions to the requirements to notify audit authorities

3.1 The current approach of the Companies Act 2006 is that the auditor should issue a statement to the company, and file it with Companies House, whenever they cease to hold office for any reason. For an audit that is not a major audit⁹, if the auditor has ceased to hold office before the end of their term of office, and if the statement explains the circumstances, a copy of the statement must then be sent by the auditor to the audit authority as their statement of the reasons. The company can also use the same statement to send to the audit authority, or provide their own.

3.2 The audit authorities' experience over the past 18 months is that large numbers of statements are sent to them which give reasons for auditors having ceased to hold office that are of little or no regulatory interest to them. The Government is therefore proposing to provide new exemptions so that, for non-major audits, the information will only have to be provided as a matter of routine in those situations where the EU Audit Directive clearly requires it, and not in certain situations, which the Directive is not intended to cover.

Departures at the end of the auditor's term of office

3.3 The EU Audit Directive only covers cases where auditors cease to hold office before the end of their term of office. So for non-major audits the Government is considering whether the auditor should also not be required to issue a statement to the company (or to file it at Companies House) where they have ceased to hold office at the end of their term of office.

Situations not covered by the Directive

3.4 The Government is also considering whether to reduce the information requirement further by providing additional exemptions. In cases where these applied for non-major audits, the current requirement for the auditor to issue a statement to the company, to Companies House and to the audit authorities would not apply.

3.5 Exemptions might be applied where the only reason that the auditor has ceased to hold office is that:

- the auditor has ceased to carry on business for instance due to retirement, death, ill health or insolvency;

⁹ See section 6 of this chapter for a discussion of how this proposal will be applied, in part, to companies subject to major audit.

- the company has decided to take advantage of audit exemption;
- the auditor of a parent company is to be appointed as the new auditor of a subsidiary; or,
- the company has entered into administration or liquidation.

3.6 The Government believes these exemptions are consistent with the underlying purpose of Article 38.2 of the EU Audit Directive¹⁰, which is aimed at identifying those cases where the auditor's departure may be of interest to the audit regulatory authorities for example where it is linked to a conflict with the client rather than external circumstances. There may be other circumstances suitable for the provision of exemptions, and the Government would welcome views on these.

Auditor's remaining powers in situations not covered by the Directive or at the end of their term of office

3.7 The Government considers that the auditor should always have the power to issue a statement to the company, and to require it to be circulated, if they consider the reasons why they have ceased to hold office should be drawn to the attention of the company's shareholders and creditors. This power would therefore still be available to the auditor at the end of their term of office, and where the proposed exemptions applied. Where the auditor exercised this power they should also file the statement with Companies House. The Government would propose the statement should also be sent to the audit authorities.

3.8 The Government would welcome views on whether, for non-major audits, statements should still be filed with Companies House in cases where the auditor does not consider they need be brought to the attention of shareholders and creditors. If the auditor does not consider the statements need be circulated, they may not need to be a matter of public record.

Question - Do you agree that, for non-major audits, the requirements for the statements to be sent to companies, Companies House and the audit authorities, should be pared back so that:

(a) they do not apply when the auditor leaves office at the end of their term of office?

¹⁰ Article 38.2 is given context by the remainder of Article 38 and by the second sentence of recital (22) to the Directive: "In order to protect the independence of the auditor it is important that dismissal should be possible only where there are proper grounds and if those grounds are communicated to the... authorities responsible for public oversight".

(b) they do not apply in some routine situations where the auditor leaves office during their term?

...unless the auditor wishes the statement to be brought to the attention of shareholders and creditors?

4. Removing the requirements for notifications to be passed on to accounting authorities

4.1 The Companies Act 2006 currently requires¹¹ the audit authorities to notify the accounting authorities of all the notifications they have received of auditors ceasing to hold office. Both the accounting authorities now agree that these notifications are not needed.

4.2 The notifications have taken the form of lists provided on a monthly basis by each of the audit authorities. The audit authorities all agree that the administration involved in preparing these lists, and providing them to the accounting authorities represents an administrative burden on them, which it might be appropriate to remove.

4.3 The Government is proposing that the requirement should be repealed. It considers, however, that the provision¹² which allows the audit authorities to decide whether to send a particular statement of reasons to the accounting authorities, should be retained. Certain statements may suggest the existence of accounting or other irregularities requiring investigation, and assuming the process for identifying these is not an excessive burden on the bodies concerned, the Government would wish to maintain this facility.

Question – Do you agree that the requirement for the audit authorities to notify the accounting authorities in every case where it receives a statement of an auditor ceasing to hold office can be repealed?

¹¹ See section 524(1)(a) of the Companies Act 2006

¹² See section 524(1)(b) of the Companies Act 2006

5. Departures of auditors for major audits

5.1 The Government has considered whether the possible simplifications it has developed for reducing the administrative burden of the system of notifications of auditors ceasing to hold office should be applied to major audits¹³. Broadly speaking, major audits are those of companies (as well as some other entities¹⁴) in which there is a significant public interest. Companies that are listed on the London Stock Exchange are an obvious example. The audit authorities issue guidance under chapter 4 of Part 16 of the Companies Act 2006 on companies that should be treated as subject to major audit¹⁵.

5.2 This issue was considered in 2005 by the Audit Quality Forum under the auspices of the ICAEW. The Forum's report¹⁶ identified changes that should be made to the framework of notifications of auditors ceasing to hold office (for major audits) with the re-enactment of the relevant provisions in the Companies Act 2006 and the implementation of the EU Audit Directive.

5.3 Given the views expressed in 2005, which influenced the detail of the provisions in the Companies Act 2006, the Government has not come to a firm conclusion on whether there should be any changes to the arrangements for major audits. The Government would be interested to hear the opinions of stakeholders on whether they now hold views similar to those expressed in 2005, or whether they feel, in the light of experience, there is scope for change. The essential features of the current framework are as follows. As previously, (UK) indicates where this is a UK originating provision and (EU) indicates it originates from the EU Audit Directive:

- When an auditor resigns or is removed by resolution of the members of a company, the company must notify Companies House (UK).

¹³ For a discussion of the current definition of "major audit" in section 525(2) of the Companies Act 2006, see section 8 of this chapter. It explains the Government's proposals for applying those of the current provisions of chapter 4 of Part 16 that apply to audits of "quoted companies" to major audits instead. In this section, major audits should be taken to be synonymous with audits of quoted companies.

¹⁴ Chapter 4 of Part 16 of the Companies Act 2006 only applies directly to UK companies. It is also applied to limited liability partnerships, some of which are subject to major audit, by regulations under the Limited Liability Partnerships Act 2000. Other similar provisions apply to other entities not directly covered by this consultation.

¹⁵ The POB's guidance is contained in each of its flowcharts (for companies and auditors) on the operation of the notice framework at - www.frc.org.uk/pob/regulation/notification.cfm. www.frc.org.uk/pob/publications/pub2030.html

¹⁶ The Audit Quality Forum report *Shareholder involvement – Auditor resignation statements* is available at: www.icaew.com/index.cfm/route/139477/icaew_ga/PDF.

- The auditor must deposit a statement with the company of the circumstances connected with ceasing to hold office (UK).
- Unless a court rules that the auditor's statement is seeking publicity for defamatory material, the company must circulate the statement of circumstances to members, and the auditor must send it to Companies House (UK).
- The auditor must file a statement of reasons for their departure with the audit authority (EU) even when they cease to hold office at the end of term (UK). This will be the same statement of circumstances mentioned above.
- The company must file a statement of reasons with the audit authority if the departure was before the end of the auditor's term of office (EU). This may be the same statement of circumstances mentioned above, though the company may submit its own statement.
- The audit authority must notify the accounting authorities of the notices it receives of auditor's departure, and may forward the statements of reasons to the accounting authorities (UK).

5.4 With any more significant changes that could be made, the Government is considering two changes to remove limited burdens on companies subject to major audit:

- The Government would welcome views on whether the company should have to send a statement of reasons to the audit authority in cases not covered by the EU Audit Directive. In line with the EU Audit Directive, companies already only have to file a statement where the auditor ceases to hold office before the end of their term of office. The new exemptions we have proposed in section 3 of this chapter could also be applied to all company statements to the audit authorities, where the company is subject to major audit.
- The Government would also welcome views on whether the companies subject to major audit need continue to be required to notify Companies House when it removes an auditor from office or the auditor resigns. This possible change is discussed in section 6 of this chapter. The more valuable filing with Companies House appears to be that from the auditor.

Question – Do you consider that the current regulatory framework for notifications of auditors ceasing to hold office, as it applies to auditors for major audits, should be maintained in its current form or is there scope for change?

Do you consider that the current framework, as it applies to companies subject to major audit, should be amended to reduce the regulatory burden?

6. Removing the requirements for companies to notify Companies House

6.1 The requirements for companies to notify Companies House when an auditor resigns or is removed from office are regulatory burdens which we consider it might be possible to remove. The auditor's statement, which the auditor must file at Companies House, appears to be a more reliable form of notification as the auditor has less reason to delay or avoid sending it. It is also more useful in terms of its content. These requirements are not covered by the EU Audit Directive, so there is some flexibility for amendment or removal.

6.2 Under this approach, the requirements for the company to notify Companies House, where an auditor resigns, or is removed from office, might be removed. These are two separate requirements in the Companies Act 2006, covering the two main circumstances in which auditors leave office before the end of their term of office. There may be different arguments for or against the removal of each. The Government is keen to seek views as to what information should continue to be placed on the Companies House register and how immediately it should be made available after an auditor has resigned or been removed from office. Unless there are reasons for the information to be available very quickly (the current requirements envisage the information being available within two weeks) the Government considers it may be preferable to rely on the auditor's statement, which arrives later.

6.3 It should be clear that, if this approach were followed, the Companies House register would only contain statements from auditors, where they had ceased to hold office, and not from companies. Alongside this, the Government's view would be that there should be no change to the provisions allowing the company to apply to the court for a direction that copies of the statement should not be circulated or filed with Companies House. The court should continue to be able to give this direction if it is satisfied that the auditor is using the statement to secure needless publicity for defamatory matter. In this case a copy of the statement will still be sent to the audit authority in confidence, as at present.

Question – What uses are you aware are made of the information required to be provided to Companies House by companies when auditors leave office?

Do you agree that there is scope for removing the requirements for the company to notify Companies House of:

- (i) resolutions for the removal of auditors?**
- (ii) resignations of auditors?**

7. Simplifying the legislation by streamlining definitions

7.1 The preceding sections of this document have set out more detailed changes that could usefully simplify the notification requirements where auditors cease to hold office. There are two further proposals which the Government considers should be introduced to support these and ensure the whole chapter 4 of Part 16 framework works effectively in a streamlined way.

Amending the requirement for the auditor to submit a statement of circumstances

7.2 At present there are several requirements for a statement from the auditor and company of the reasons or circumstances around the auditor's departure. The auditor must deposit a statement with the company, which may set out the circumstances connected with their ceasing to hold office, then file that statement with Companies House. The company and auditor are also required to notify the audit authority of the reasons for the auditor's departure, which, for the auditor, must be the statement of circumstances if these were set out. It would seem sensible to simplify these provisions so that it is clear that there should be just one statement of reasons, which can be used to meet all these requirements.

7.3 The statement would therefore have to give the auditor's reasons for ceasing to hold office in all cases, in order to comply with EU law. If the proposals in section 3 of this chapter were accepted, for non-major audits the statement would also say whether the reasons should be drawn to the attention of shareholders and creditors. For major audits the statement would have to be circulated to shareholders and creditors in all cases, as at present. Statements circulated to shareholders and creditors would then be filed at Companies House (subject to the existing protection from defamation). In effect the statement would be the default statement of reasons. In many cases it would be the only statement required as the company, upon receiving it from the auditor, may be content to send a copy to the audit authority as its own statement of reasons.

7.4 The Government has noted the discussion in the report of the Audit Quality Forum about whether legally a statement of reasons is different to a statement of circumstances. However the Companies Act 2006 treats a statement of circumstances as sufficient for the EU Audit Directive's requirement for a statement of reasons. The Government also generally prefers to use Directive terminology when implementing EU obligations. However the Government would welcome views on whether the obligations should refer to reasons or circumstances.

Distinction between quoted and unquoted companies and major and non-major audits

7.5 The Government is also considering a further simplification. At present in some parts of the provisions, a distinction is drawn between quoted companies and unquoted companies. In other parts of the provisions, a similar distinction is drawn between companies subject to major audit and other companies. The Government is seeking views on whether one distinction, between companies subject to major audit and other companies, could be used throughout the provisions.

Question - Do you support the idea of simplifying the information requirements by:

- a) providing that one statement of reasons by the auditor should be required for the purposes of sending to the company and to the audit authorities?**

- b) replacing the distinction between quoted and unquoted companies with a distinction between major and non major audits?**

8. Summary of new system

8.1 In order to assist readers to assess the impact of the measures discussed in this paper, there follows a brief description of how the notifications system should work in the event that all the proposals discussed are agreed and implemented. This should not be read as saying that the Government has concluded this is the way forward; that will depend on the outcome of the consultation, and legislative opportunities. It may well be that only some of the proposals are implemented. The purpose of this is simply to aid comprehension.

Basic procedure

8.2 When an auditor departs and it is a notifiable departure, they must:

- notify the audit authority, and that notification must be accompanied by a statement of the reasons for their ceasing to hold office; and,
- provide the company with a copy of that statement.

For a non-major audit, the auditor may also require the company to circulate the statement to the people who are entitled to be sent copies of the accounts.

8.3 When it receives this statement, for a notifiable departure, the company must - either:

- send the statement as its own statement of the reasons why the auditor ceased to hold office; or,
- provide its own statement of the reasons.

8.4 For all major audits, or for non-major audits where the auditor has required it, the company must circulate the statement to those entitled to receive copies of the accounts. The company must either do so within 14 days (and the auditor must file the statement at Companies House), or apply to the court. If the court rules that the statement is defamatory, it need not be sent out. If the court declines to make such a ruling, the statement must be sent out within 14 days of the decision (and the auditor must then file it at Companies House).

8.5 The audit authority may forward details of the reasons on to the accounting authorities but would not be obliged to do so.

Notifiable departures

8.6 A notifiable departure (for a non-major audit) is one where the auditor departs before the end of their term of office, and is not covered by one of the following exemptions:

- auditor going out of business, death of auditor, ill health or retirement of auditor
- the company taking advantage of audit exemption
- the company is a subsidiary and is part of a group change of auditor
- the auditor is leaving because the company is becoming insolvent

8.7 In respect of the auditor's obligations, all departures are notifiable departures for major audits. However the Government would maintain the current exception for companies subject to major audit, so that they do not have to notify the audit authority when the auditor leaves office at the end of his term of office. Further to this, the company would not have to notify the audit authority of a departure from a major audit where one of the exemptions under paragraph 8.6 applied, as for non-major audits.

Auditor's right to require circulation for non-notifiable departures

8.8 Even in a departure that is not a notifiable departure, the auditor may require the company to circulate a statement of their reasons to the persons entitled to receive the company's accounts. Subject to the anti-defamation provisions, this should also be filed with Companies House and the audit authorities.

Question – In conclusion, do you consider that the resulting framework:

(a) is simpler and less burdensome for non-major audits?

(b) strikes the right balance between regulation and simplification for major audits?

7. Consultation questions

A text file containing these questions is available on the BIS website at www.bis.gov.uk/consultations

1. Do you agree that, for non-major audits, the requirements for the statements to be sent to companies, Companies House and the audit authorities should be pared back so that:

(a) they do not apply when the auditor leaves office at the end of their term of office?

(b) they do not apply in some routine situations where the auditor leaves office during their term?

...unless the auditor wishes the statement to be brought to the attention of shareholders and creditors?

2. Do you agree that the requirement for the audit authorities to notify the accounting authorities in every case where it receives a statement of an auditor ceasing to hold office can be repealed?

3. (a) Do you consider that the current regulatory framework for notifications of auditors ceasing to hold office, as it applies to auditors for major audits, should be maintained in its current form or is there scope for change?

(b) Do you consider that the current framework, as it applies to companies subject to major audit, should be amended to reduce the regulatory burden?

4. (a) What uses are you aware are made of the information required to be provided to Companies House by companies when auditors leave office?

(b) Do you agree there is scope for removing the requirements for the company to notify Companies House of:

(i) resolutions for the removal of auditors?

(ii) resignations of auditors?

- 5. Do you support the idea of simplifying the information requirements by:**
- a) providing that one statement of reasons by the auditor should be required for the purposes of sending to the company and to the audit authorities?**
 - b) replacing the distinction between quoted and unquoted companies with a distinction between major and non major audits?**
- 6. In conclusion, do you consider that the resulting framework:**
- (a) is simpler and less burdensome for non-major audits?**
 - (b) strikes the right balance between regulation and simplification for major audits?**
- 7. Do you agree with the costs and benefits itemised in the Impact Assessment at Annex C? Can you provide any supporting evidence?**

What happens next?

We will publish the Government Response to this consultation, within three months of the close of this consultation on 20 January. This will be available on the BIS website at:

www.bis.gov.uk/consultations

Should these proposals be supported at consultation it will then be necessary to identify a suitable legislative vehicle. This may affect what in this package of proposals can ultimately be delivered.

Annex A: The Consultation Code of Practice Criteria

1. Formal consultation should take place at a stage when there is scope to influence policy outcome.
2. Consultation should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
3. Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
4. Consultation exercise should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
5. Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
6. Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
7. Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

Comments or complaints

If you wish to comment on the conduct of this consultation or make a complaint about the way this consultation has been conducted, please write to:

Tunde Idowu,
BIS Consultation Co-ordinator,
1 Victoria Street,
London
SW1H 0ET

Telephone Tunde on 020 7215 0412
or e-mail to: Babatunde.Idowu@bis.gsi.gov.uk

Annex B: List of Individuals / Organisations consulted

This consultation document will be sent to those on the following list. We shall also draw it to the attention of the approximately 800 interested parties who have chosen to be on the circulation list of the Corporate Law and Governance Directorate of the Department for Business, Innovation and Skills.

Association of British Insurers

Association of Chartered Certified Accountants (ACCA)

Association of Authorised Public Accountants (AAPA)

British Chambers of Commerce

Confederation of British Industry

Deloitte

Ernst and Young

Financial Reporting Review Panel

Financial Services Authority

Institute of Chartered Accountants for England and Wales (ICAEW)

Institute of Chartered Accountants of Ireland (ICAI)

Institute of Chartered Accountants of Scotland (ICAS)

Institute of Chartered Secretaries and Administrators (ICSA)

Institute of Directors

Investment Management Association

KPMG

Law Society

Law Society of Northern Ireland

Law Society of Scotland

National Association of Pension Funds

Northern Ireland Chamber of Commerce and Industry

Price Waterhouse Coopers

Professional Oversight Board of the Financial Reporting Council

UK Shareholders' Association

Annex C – Impact Assessment

Summary: Intervention & Options

Department /Agency: BIS	Title: Impact Assessment for consultation on notices of auditors leaving office - simplification for companies and auditors	
Stage: consultation	Version: 1	Date: November 2009
Related Publications: Notices of Auditors Leaving Office		

Contact for enquiries: Paul Smith (tel: 020 7215 4164)

What is the problem under consideration? Why is government intervention necessary?

The current system for notifying the departure of an auditor is overly complex. Both companies and auditors, in certain circumstances, must send statements to both the audit authorities and to Companies House. BIS has received feedback from the audit authorities that the current system is a significant administrative burden but provides only limited benefit.

Any amendments to simplify this process must be compatible with EU directive 2006/43/EC.

What are the policy objectives and the intended effects?

To simplify the notification and information requirements around the departure of auditors while retaining compatibility with EU directive 2006/43/EC. This could be done by:

- Removing the requirement for companies to inform Companies House of auditors leaving office and therefore reduce duplication of the notifications, while retaining option for auditors to notify if they believe circumstances require;
- Minimising the cases where notifications have to be sent to explain reasons for the auditors departure that are of no interest to shareholders and creditors or the audit authorities.

What policy options have been considered? Please justify any preferred option.

1. Do nothing.
2. Simplify the reporting requirements associated with the departure of auditors.

When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects? - 2 years after implementation

Ministerial Sign-off For consultation stage Impact Assessments:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister:

Date:

Summary: Analysis & Evidence

Policy Option: 1 Description: Do nothing

COSTS	ANNUAL COSTS		Description and scale of key monetised costs by 'main affected groups'	
	One-off (Transition)	Yrs		
	£ 0			
	£ 0		Total Cost (PV)	£ 0
Other key non-monetised costs by 'main affected groups'				

BENEFITS	ANNUAL BENEFITS		Description and scale of key monetised benefits by 'main affected groups'	
	One-off	Yrs		
	£			
	£		Total Benefit (PV)	£
Other key non-monetised benefits by 'main affected groups'				

Key Assumptions/Sensitivities/Risks

Price Base Year 0	Time Period Years 0	Net Benefit Range (NPV) £ 0	NET BENEFIT (NPV Best estimate) £ 0
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What is the geographic coverage of the policy/option?		UK		
On what date will the policy be implemented?		N/A		
Which organisation(s) will enforce the policy?		Companies Hse / Audit Authorities		
What is the total annual cost of enforcement for these		£ not known		
Does enforcement comply with Hampton principles?		Yes		
Will implementation go beyond minimum EU requirements?		Yes		
What is the value of the proposed offsetting measure per year?		£ 0		
What is the value of changes in greenhouse gas emissions?		£ 0		
Will the proposal have a significant impact on competition?		No		
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

Impact on Admin Burdens Baseline (2005 Prices) TBC (Increase - Decrease)

Policy Option: 2	Description: Simplifying the reporting requirements associated with departure of auditors
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COSTS	ANNUAL COSTS	Description and scale of key monetised costs by 'main affected groups' This policy aims to remove costs.		
	One-off (Transition) Yrs			
	£ 0			
	Average Annual Cost			
	£ 0			
	Total Cost (PV)			£ 0
Other key non-monetised costs by 'main affected groups': We are seeking views on whether the delay in information on the Companies House register may have associated costs.				

BENEFITS	ANNUAL BENEFITS	Description and scale of key monetised benefits by 'main affected groups' Consisting of: Reduced notification to audit authorities - £300,000; Reduced notification to Companies House - £880,000 (proposals c and e); Reduced admin burden for audit authorities - £75,000		
	One-off Yrs			
	£			
	Annual Benefit			
	£ 0- £1,255,000			
	Total Benefit (PV)			£0- £10.4m
Other key non-monetised benefits by 'main affected groups' Better understanding of legal requirements by auditors and companies due to simpler law.				

Key Assumptions/Sensitivities/Risks

Total benefits would depend on which proposals come into effect. The max range is based on the implementation of proposals a, b, c and e under Option 2. Discount rate of 3.5% (10 year period). Increased risk that change of auditors caused by dispute between company and auditor will not be notified.

Price Base Year 0	Time Period Years 0	Net Benefit Range (NPV) £ 0-£10.4m	NET BENEFIT (NPV Best estimate) £ 0
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	TBC – Earliest October 2010			
Which organisation(s) will enforce the policy?	Companies Hse / Audit Authorities			
What is the total annual cost of enforcement for these organisations?	£ not known			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	Yes			
What is the value of the proposed offsetting measure per year?	£ 0			
What is the value of changes in greenhouse gas emissions?	£ 0			
Will the proposal have a significant impact on competition?	No			
Annual cost (£-£) per organisation(excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A
Impact on Admin Burdens Baseline (2005 Prices): TBC			(Increase - Decrease)	

Evidence Base (for summary sheets)

PROPOSAL

1. To simplify the notification and information requirements around the departures of auditors.

OBJECTIVE

2. To reduce the administrative burden on companies, auditors, audit authorities and accounting authorities, while ensuring compliance with Directive 2006/43/EC.

BACKGROUND

3. Chapter 4 of Part 16 to the Companies Act 2006, covers the removal, resignation and non-reappointment of auditors and provides a framework in which shareholders, audit authorities, Companies House, accounting authorities and creditors are informed, where necessary, of the circumstances in which an auditor has ceased to hold office. Both auditors and companies have a role in providing this information:

4. **Auditors** are currently required to issue a statement to the company whenever they cease to hold office. This should either state that there are no circumstances that need be drawn to the attention of the company's shareholders; or set out those circumstances. For quoted companies, the statement should always set out the circumstances. The auditor must then send a statement to the relevant audit authority of the reasons why they ceased to hold office. Where the auditor's statement to the company has set out the circumstances in which they ceased to hold office, the auditor should send this statement to the appropriate authority. Where the auditor ceased to hold office at the end of their term of office, the statement to the audit authority is not required unless the audit is a major audit.

5. Currently **Companies** must notify Companies House whenever an auditor is removed or resigns from office. When it then receives a statement from the auditor under section 519 of the circumstances in which the auditor ceased to hold office, the company may send that onto the audit authority as its statement of reasons, under section 523. However, if it prefers, or if the auditor's statement under s519 does not state any circumstances that need to be drawn to the attention of the shareholders, the company must provide the audit authority with its own statement of reasons. The company is obliged to notify both Companies House and the audit authority that the auditor has ceased to hold office.

6. The Companies Act 2006 increased the range of cases in which companies and auditors must issue a statement of why auditors have ceased to hold office. For the first time, the Act made requirements for statements to be sent by companies and auditors to the appropriate audit authorities. Feedback we have received from them

suggests the changes have introduced additional administrative burdens, with only limited benefits and that compliance is patchy, especially by companies.

7. We understand that between them, the audit authorities currently receive in the region of 10,000 notifications per year from auditors, though the number from companies is considerably lower while Companies House receives 8,600 notifications a year. In many cases the reasons that the auditor has ceased to hold office appear to be routine, including a decision by the company to take advantage of audit exemption or change to an auditor who also audits a parent company.

Options for implementing

OPTION 1: Do Nothing.

8. Do nothing is a viable option but it retains the current duplication of notification.

OPTION 2: Simplify the reporting requirements associated with departure of auditors.

9. A package of measures to reduce the levels of duplication and notification. The following proposals are set out in the consultation.

Proposal a) Remove the requirement to notify audit authorities, companies and Companies House when the auditor leaves office before the end of his term for the following situations:

- Death, illness, retirement or closure of audit firm;
- Companies choosing to take advantage of audit exemption
- Companies going into administration or liquidation;
- Change of auditor of a subsidiary to auditor of parent company

Proposal b) Remove the requirement for the audit authority to notify the accounting authority in all cases of auditor departure.

Proposal c) Remove requirement on the company to file with Companies House when the auditor resigns, or is removed by resolution.

Proposal d) Moving to a uniform format for statements to the audit authority and the company (members, creditors and Companies House).

Proposal e) To allow the auditor to state whether the reasons need to be drawn to the attention of the shareholders and creditors of the company, and only to require filing with Companies House where the auditor considers that the reasons should be circulated (this is discussed in sections 3 and 7 of chapter 6 of the consultation document).

COSTS AND BENEFITS

Option 1 –Do nothing: *Costs & Benefits*

10. There will be no direct costs or benefits if UK legislation is left unchanged.

Option 2 – Simplify the reporting requirements associated with departure of auditors.

Costs

11. Proposal a - to remove the requirement to notify when the auditor leaves office before the end of their term for specified reasons.

12. We do not anticipate any new costs arising as this will result in a reduction in the requirement to notify.

13. Proposal b - remove the requirement for the audit authority to notify the accounting authority in all cases of auditor departure.

14. We do not anticipate any new costs arising as this will directly reduce an administrative burden.

15. Proposal c - remove requirement on the company to file with Companies House when the auditor resigns, or is removed by resolution.

16. We do not anticipate any new costs arising as this will result in a reduction in the number of notifications to Companies House. We are seeking views on whether the delay in availability of this information on the Companies House register may have associated costs (possibly not quantifiable).

17. Proposal d - Moving to a uniform format for statements to the audit authority and the company (members, creditors and Companies House).

18. This removes the current situation providing for a statement of circumstances in places and a statement of reasons for the auditor's departure in others. We do not anticipate this proposal will result in any additional costs to the company or the auditor as this option does not result in an additional burden. A full statement of reasons was required in all cases by the audit authorities, as will be the case now.

19. Proposal e - to remove further burdens for non-major audits by allowing the auditor to state whether the reasons need to be drawn to the attention of the shareholders and creditors of the company, and only to require filing with Companies House where the auditor considers that the reasons should be circulated.

20. We do not anticipate any new costs arising as this proposal will directly reduce the administrative burden. We are seeking views on whether the non-availability of this information on the Companies House register may have associated costs

(possibly not quantifiable). As the information will only be the reasons for the auditor leaving office, which the auditor considers need not be circulated to shareholders and creditors, and which are not currently available on the register, the costs are likely to be limited.

Benefits

21. The key benefits will be a simplified notification process supported by simplified law which will be easier for auditors and companies to understand.

22. Proposal a - to remove the requirement to notify when the auditor leaves office before the end of their term for specified reasons.

23. We anticipate that approximately 1/2 of the current notifications currently filed give the reasons outlined in paragraph 9. As the audit authorities receive approximately 12,000 (10,000 from auditors and 2,000 from companies) notifications a year at an estimated cost of £50 per notification, this amounts to a saving of £300,000/year who will not incur administrative and legal costs.

Cost Savings to companies:	£50,000
Cost Savings to auditors:	£250,000

24. Proposal b - remove the requirement for the audit authority to notify the accounting authority in all cases of auditor departure.

25. This will result in a significant reduction in administration for the audit authorities. We estimate savings to the audit authorities that are equivalent of one and a half full time equivalent employees at £75,000.

Total Cost Saving to audit authorities: £75,000

26. Proposal c - remove requirement on the company to file with Companies House when the auditor resigns, or is removed by resolution.

27. Companies House receive 8,600 notifications a year at an estimated cost of £50 per notification, this amounts to a saving of £430,000.

Total Cost Saving to companies: £430,000

28. Proposal d - Moving to a uniform format for statements to the audit authority and the company.

29. There will be an administrative saving for auditors, where they need to submit notifications to both Companies House and the audit authorities, and to companies notifying the audit authorities. Currently, different types of statement must be filed with Companies House and the audit authorities. By introducing a uniform statement, there will be a saving in administrative costs. There will also be a saving for

companies who will be able to use auditor statements more often as they will always give reasons why the auditor ceased to hold office. We have not estimated this figure as it may be negligible.

30. Proposal e - to remove further burdens for non-major audits by allowing the auditor to state whether the reasons need to be drawn to the attention of the shareholders and creditors of the company, and only to require filing with Companies House where the auditor considers that the reasons should be circulated.

31. The audit authorities receive approximately 10,000 notifications from auditors a year. As the majority (perhaps 95%) relate to non-major audits; we anticipate that approximately 750 notifications a year (500 relating to major audits with 250 others) will be lodged with Companies House. In total, we estimate there will be a reduction of 9,250 notifications to Companies House with an estimated cost of £50 per notification amounting to a saving of £450,000).

Total Cost Savings to auditors: £450,000

32. The benefits for the above proposals have been itemised separately so there is duplication. If, following the consultation, the decision is to implement in full, then the cumulative total will be reduce appropriately.

33. If proposals a to e were implemented, the cost savings from the reduction in notifications to the audit authorities would amount to £300,000 (proposal a). Proposal b would result in savings to the audit authorities of £75,000. Proposal c would lead to further cost savings to companies of £430,000. Proposal e would result in cost savings to auditors equivalent to £450,000. The total cost savings to companies, auditors and audit authorities would amount to approximately £1.3 million per year.

Options	Filing requirements for Companies (at present)		Filing requirements for Auditors (at present)	
	Statement to Companies House	Statement to audit authority	Statement to the company/Companies House	Statement to audit authority
Do Nothing	No change	No change	No change	No change
Proposal (a)	Significant reduction	Significant reduction	No change	Significant reduction
Proposal (b)	Remove requirement	No change	No change	No change
Proposal (c)	No change	No change	No change	Remove requirement
Proposal (d)	Uniform statements	Uniform statements	Uniform statements	Uniform statements
Proposal (e)	No change	No change	Significant reduction	No change

RISKS

32. A possible consequence of reducing the level of notification is an increase in the risk that change in auditors are caused by disputes between the company and auditor will not be notified.

WHO WILL BE AFFECTED?

33. Auditors, Companies, Companies House, Audit Authorities and Accounting Authorities.

EQUALITIES IMPACT TESTS

34. We have considered three equalities impact tests (gender, race, disability). After initial screening as to the potential impact of this policy/regulation on race, disability and gender equality it has been decided that there will not be a major impact upon minority groups in terms of numbers affected or the seriousness of the likely impact.

SMALL FIRMS IMPACT TEST

35. There is no change in nature of number of overall population of companies affected by these provisions.

ENFORCEMENT AND SANCTIONS

36. No new enforcement or sanctions have been introduced.

CONSULTATION

37. Consultation paper (09/1485) was published on 25 November 2009.

COMPETITION ASSESSMENT

38. The competition filter has been applied. It is considered that these changes will not give rise to disproportionate costs of entry or administrative costs for either small or large business. This change is not anticipated to restrict innovation in sectors characterised by rapid technological change and would not impair freedom to provide services.

QUESTIONS

39. Do you agree with the costs and benefits itemised in this impact assessment, can you provide any evidence to cause adjustments to be made.

Specific Impact Tests: Checklist

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Y	N
Small Firms Impact Test	Y	N
Legal Aid	N/A	N
Sustainable Development	N/A	N
Carbon Assessment	N/A	N
Other Environment	N/A	N
Health Impact Assessment	N/A	N
Race Equality	Y	N
Disability Equality	Y	N
Gender Equality	Y	N
Human Rights	N/A	N
Rural Proofing	N/A	N

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